would impose a costly and complex regulatory system, which will not more efficiently or effectively ensure just and reasonable rates. In this regard, there are substantial questions about the reliability of the estimated fair market analysis and the inherent inconsistency in the prevailing price test. Moreover, the proposed rules would severely limit the efficiencies and economies of scale available under the current rules. Thus, since the Commission recently affirmed that the current cost allocation and affiliate transaction rules effectively protect the ratepayers, they should be maintained.[49]

III. Miscellaneous Issues.

In the NPRM the Commission proposes several additional changes to the cost allocation and affiliate transaction rules, regarding their implementation. Ameritech will address some of these issues below.

A. The Commission should allow LECs to use different rates of return for affiliate transactions.

In the NPRM, the Commission proposes to limit the rate of return used in calculating the return on investment in affiliate transactions to the rate of return of 11.25 percent.[50] The Commission also seeks comment on whether the rate of return component should vary depending upon the type of regulation applied to the carrier, i.e., price caps verses cost-plus regulation, and whether the rate of return component should be a function of the return component allowed by both the state and federal commissions.

In this regard, any number of rate of return components may be reasonable. Specifically, those carriers regulated under price caps should be allowed to choose a rate within the reasonable range of rates established by the

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[49] Based on the evidence provided in these comments, the Commission in fact should revisit these cost allocation and affiliate transaction rules and streamline them to make them more consistent with current industry developments.

[50] NPRM at ¶¶ 66-71.

Commission. In addition, other carriers may want to use a weighted average of their interstate and intrastate rates of return because affiliate transactions with rare exception support both the state and federal jurisdictions. Thus, mandating the use of one method of rate of return component unnecessarily constrains carriers from using the rate most suitable for the transaction and justifying the circumstances supporting that rate. Thus, carriers should have the flexibility to use a different rate of return component provided it is reasonable and disclosed in their cost allocation manual.[51]

B. The Commission should maintain its generic rate base methodology.

In the NPRM, the Commission seeks comment on its proposal to further define its generic rate base methodology to limit the items which could be included by an affiliate in its determination of the fully distributed costs of a transaction with the carrier. Essentially, the Commission proposes to impose the specific Part 65 rate base calculation requirements on nonregulated affiliates to ensure that the affiliate transaction costs are not overstated.[52] In this regard, the Commission proposes that affiliates exclude all property, plant and equipment which is not used and useful, treat all plant under construction as proposed in the Allowance for Funds Used During Construction NPRM,[53] and exclude other items, such as customer deposits, unfunded accrued pension costs, and unamortized debt issuance expense, that are currently excluded from the regulated rate base.

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[51] See Letter from Jose'-Luis Rodriguez, Chief, Audits Branch, Common Carrier Bureau, Federal Communications Commission to Mr. Fred Konrad, Director - Federal Regulatory Matters, Ameritech Corporation, dated April 20, 1992.

[52] See NPRM at ¶¶ 58-65.

[53] See Accounting and Ratemaking Treatment for the Allowance for Funds Used During Construction (AFUDC), Notice of Proposed Rulemaking, 8 FCC Rcd. 2084 (1993).

Through this proposal, the Commission again seeks to impose a rigid and complex regulatory system on nonregulated affiliates without providing reasonable justification. The current generic rate base provides sufficient protection to ratepayers by ensuring just and reasonable rates. Specifically, the generic rate base that was developed by the United States Telephone Association (USTA) with participation from the Commission staff has worked for two years without there being a finding that any improper costs were included in affiliate transactions. Moreover, the formulation of the generic rate base, by relying on the generally acceptable accounting principles, provides sufficient constraints on affiliates from any inappropriate accounting treatment. The generic rate base formula is also measurable and auditable.

Furthermore, the rules established under Part 65 applicable to regulated carriers are not easily adaptable to nonregulated affiliates. Since these affiliates do not use the Part 32 accounting structure, superimposing those rate base rules to a different accounting structure is inappropriate and could be misleading due to the different accounting classifications used. Similarly, superimposing the Commission's rules regarding construction projects is fundamentally flawed because nonregulated affiliates deploy and retire assets under a different methodology and also are not subject to the Commission's depreciation prescription.

Finally, as mentioned above, other factors such as price caps, increasing competition and Computer III provide overwhelming incentives for LECs to act efficiently. Therefore, imposing the specific Part 65 rate base rules on affiliate transactions is unnecessary and costly, and does not provide any benefits.

C. The Commission must include all the costs of changing its cost allocation and affiliate transaction rules in any exogenous cost change.

In the NPRM, the Commission states that because its proposed changes to the cost allocation and affiliate transaction rules constitute changes to the Uniform System of Accounts (USOA), and the Commission has determined that changes to the USOA "should generally" be treated as exogenous, adoption of the proposed rules would result in an exogenous cost change to LECs' price caps.

While Ameritech does not automatically agree that these changes should result in an exogenous cost change, if the Commission does require an exogenous cost change it must include the increased regulated costs generated by the adoption of the rules. As set forth above, adoption of the rules would involve the increased costs of establishing and maintaining mechanisms to calculate an estimated fair market value for practically every affiliate transaction, the increased costs to change the billing systems and ARMIS, and the increased costs of the annual independent Part 64 audit. Since all of these costs emanate from the change to the USOA, they should be included in any exogenous cost calculation.

IV. Conclusion.

As outlined above, Ameritech opposes the changes proposed in the NPRM. Based on the foregoing, the Commission should reject the proposed rules, and work to streamline its current cost allocation and affiliate transaction rules, due to the substantial protections from competition and industry changes. In the first instance, there are several developments in the telecommunications industry -- price caps, increasing competition and Computer III -- which in and of themselves will ensure just and reasonable rates. Secondly, the proposed rules would impose a costly and complex regulatory system, which will not more efficiently or effectively ensure just and reasonable rates. In this regard, there are substantial questions about the reliability of the estimated fair market analysis and the inherent inconsistency in the prevailing price test. Moreover, the proposed rules would severely limit the efficiencies and economies of scale available under the current rules. Thus, since the Commission recently affirmed that the current cost allocation and affiliate transaction rules effectively protect the ratepayers, they should be maintained.

Respectfully submitted,

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